

FDIC State Profile

Fall 2005

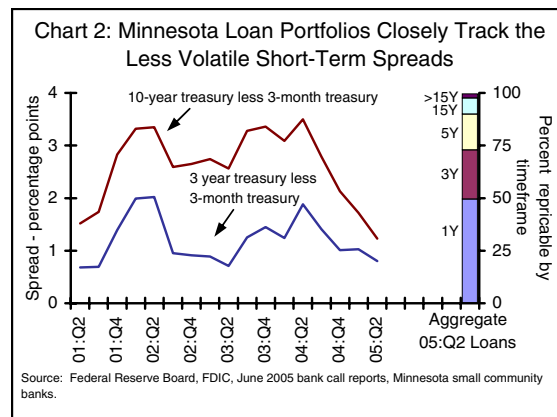
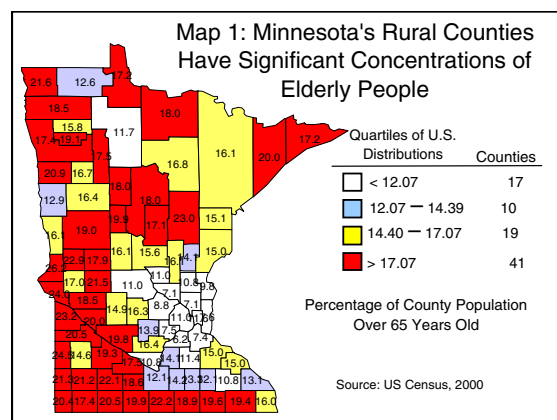
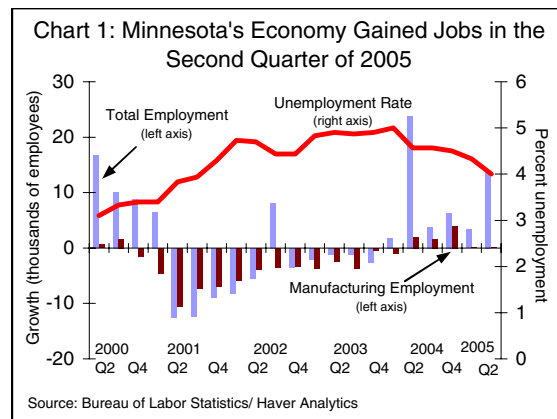
Minnesota

Minnesota's economic expansion accelerated in the second quarter of 2005.

- Minnesota's economy added more than 13,000 jobs in the second quarter, attaining a record level of 2.71 million jobs on a seasonally-adjusted basis (see Chart 1). This marks the first quarter that employment has exceeded levels reached before the downturn of 2001. However, year-over-year employment growth was less than the national rate.
- While Minnesota's manufacturing sector continues to recover slowly, having added more than 7,000 jobs in the last six quarters, it is still more than 50,000 jobs below its peak level reached in the second quarter of 1998.
- The state's unemployment rate declined to 4.0 percent in the second quarter, the lowest level since the third quarter of 2001. The improvement was broadly based, as the rate declined by 0.7 percent in **Minneapolis-St. Paul** and by more than a full percentage point in **Duluth, Rochester, and St. Cloud**.
- The recent hurricanes' effects on the Minnesota economy appear to be modest and are centered on energy. Like other states in the region, energy prices have risen sharply, but supplies have remained adequate. Farmers face substantially higher fuel costs during the harvest season.

Minnesota's rural counties have relatively large concentrations of elderly people.

- Based on 2000 Census data, 41 of Minnesota's 87 counties rank in the top quarter of the nation's counties in terms of population older than 65. All but one of these counties are rural (see Map 1).
- Large concentrations of the elderly tend to be associated with rural depopulation, as 30 of the older counties lost population between 1970 and 2000. These counties typically experience the out-migration of younger people seeking educational or employment opportunities.
- However, this population profile is distinctly different than the relatively large younger Minneapolis, St. Paul area. As a result, in the aggregate, the Census Bureau projects that by 2030, 18.9 percent of Minnesota's



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population will be older than 65, compared with 19.7 percent for the United States.

Despite a large presence of elderly in Minnesota's rural areas, rural institution core funding growth closely tracks the U.S. trend.

- Insured institutions operating in rural areas face funding challenges, especially in areas with large elderly populations. Commonly, when elderly depositors pass away, their deposits quickly move to their heirs' institutions, often located in far-away metropolitan areas.
- So far, although Minnesota's proportion of elderly counties is greater than the U.S., the state's rural core deposit base has managed to closely track the nation.

Bank earnings remain solid as rising short-term rates have offset moderate declines in term yield spreads.

- Earnings performance remains positive for most Minnesota institutions. The median return-on-assets ratio was 1.42 percent at June 2005, slightly higher than one year ago. Only 4.0 percent of institutions were unprofitable in the first half of the year.
- The declining spread between three-month and ten-year interest rates has many national banking analysts fretting about potential net interest margin (NIM) compression. However, Minnesota's small community banks do not have the long-term loan exposure that would make them highly responsive to changes in long-term rates.¹ Nearly two-thirds of community bank loans reprice within three years; therefore, margins tend to track more closely the much less volatile three-month to three-year treasury spreads (see Chart 2).
- Given the typical asset-sensitive nature of small community banks, rising short-term rates often benefit small bank margins, even when the yield curve flattens. In fact, the June 2005 median NIM in Minnesota's small community banks was 10 basis points higher than a year earlier.

Asset quality continues to improve at Minnesota's insured institutions, and loan growth is strong.

- Delinquent loans at Minnesota's insured institutions have declined for two straight years, and represented just 1.48 percent of total loans in June 2005 (see Chart 3).
- Although the state has seen a recent spike in consumer bankruptcies as a result of pending bankruptcy reform enactment, the typical Minnesota institution has very

low consumer loan exposure, and consumer loan charge-offs historically have been negligible.

- Spurred by business investment, insured institutions are experiencing strong loan growth. Commercial real estate lending was most pronounced growing a median 17.3 percent from a year earlier. Commercial business lending growth was also strong at 7.9 percent.

Prices for most of Minnesota's agricultural commodities are forecasted to decline.

- The United States Department of Agriculture (USDA) projects that Minnesota will produce its second largest corn crop in 2005, just below the record harvest in 2004. Large stocks remaining from last year's harvest will cause lower prices in the upcoming marketing year (see Table 1).
- Although the soybean harvest is projected to be more than 13 percent higher than last year, reduced yields in the rest of the country and strong demand should lead to higher prices.
- Milk prices will likely decline significantly over the next year, as large increases in production per cow improves milk supplies.

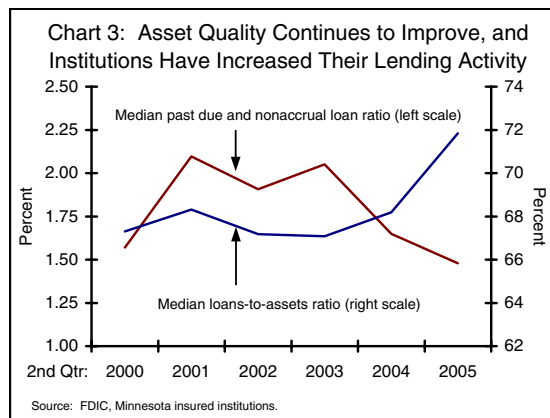


Table 1: Most Commodity Prices Are Expected to Decline in 2006

	2003	2004	Est. 2005	Forecast 2006	% of Ag Cash Receipts
Corn	2.32	2.42	2.07	2.00	18.7
Soybeans	5.53	7.34	5.80	6.00	16.8
Wheat	3.56	3.40	3.40	3.10	3.5
Cattle	84.69	84.75	85.50	79.00	10.1
Hogs	39.45	52.51	48.50	45.00	17.6
Milk	12.52	16.05	15.05	13.35	13.6

Note: Grain prices are for marketing year of each crop. Crop quantities are per bushel; livestock are per hundredweight.

Source: USDA World Agricultural Supply and Demand Estimates, August 12, 2005
USDA/Economic Research Service 2004

¹Small community banks are defined as FDIC-insured commercial banks with less than \$250 million in total assets that have been in existence at least three years. At June 30, 2005, these institutions represented 87 percent of all insured institutions in Iowa.

Minnesota at a Glance

ECONOMIC INDICATORS (Change from year ago, unless noted)

Employment Growth Rates	Q2-05	Q1-05	Q2-04	2004	2003
Total Nonfarm (share of trailing four quarter employment in parentheses)	1.1%	1.8%	0.8%	0.6%	-0.2%
Manufacturing (13%)	1.9%	2.6%	-0.8%	-0.2%	-3.5%
Other (non-manufacturing) Goods-Producing (5%)	-0.2%	1.4%	3.4%	1.1%	0.4%
Private Service-Producing (67%)	1.1%	1.9%	1.3%	1.0%	0.5%
Government (15%)	0.8%	0.9%	-0.4%	-0.3%	-0.4%
Unemployment Rate (% of labor force)	4.0	4.3	4.6	4.7	4.9

Other Indicators	Q2-05	Q1-05	Q2-04	2004	2003
Personal Income	6.0%	5.5%	8.7%	6.5%	3.8%
Single-Family Home Permits	-2.6%	-8.9%	10.0%	0.0%	18.7%
Multifamily Building Permits	-36.4%	-20.3%	16.1%	5.2%	-12.5%
Existing Home Sales	-0.6%	4.1%	16.3%	8.4%	3.3%
Home Price Index	9.3%	9.4%	9.6%	9.5%	7.4%
Bankruptcy Filings per 1000 people (quarterly annualized level)	4.44	3.78	3.66	3.50	4.17

BANKING TRENDS

General Information	Q2-05	Q1-05	Q2-04	2004	2003
Institutions (#)	470	478	485	478	486
Total Assets (in millions)	65,360	63,896	61,815	63,483	108,679
New Institutions (# < 3 years)	16	15	17	15	13
Subchapter S Institutions	305	313	293	290	269

Asset Quality	Q2-05	Q1-05	Q2-04	2004	2003
Past-Due and Nonaccrual Loans / Total Loans (median %)	1.48	1.59	1.65	1.38	1.65
ALLL/Total Loans (median %)	1.25	1.28	1.27	1.25	1.27
ALLL/Noncurrent Loans (median multiple)	2.37	2.32	1.83	2.11	1.83
Net Loan Losses / Total Loans (median %)	0.00	0.00	0.01	0.07	0.10

Capital / Earnings	Q2-05	Q1-05	Q2-04	2004	2003
Tier 1 Leverage (median %)	9.39	9.30	9.19	9.23	9.05
Return on Assets (median %)	1.38	1.37	1.42	1.32	1.24
Pretax Return on Assets (median %)	1.64	1.61	1.66	1.57	1.53
Net Interest Margin (median %)	4.49	4.38	4.40	4.37	4.33
Yield on Earning Assets (median %)	6.29	6.01	5.88	5.90	6.13
Cost of Funding Earning Assets (median %)	1.85	1.62	1.47	1.49	1.76
Provisions to Avg. Assets (median %)	0.10	0.09	0.10	0.12	0.14
Noninterest Income to Avg. Assets (median %)	0.57	0.53	0.64	0.60	0.64
Overhead to Avg. Assets (median %)	3.03	2.95	3.00	3.03	3.05

Liquidity / Sensitivity	Q2-05	Q1-05	Q2-04	2004	2003
Loans to Assets (median %)	71.8	70.2	68.2	69.1	65.9
Noncore Funding to Assets (median %)	17.5	15.6	14.5	14.9	13.0
Long-term Assets to Assets (median %, call filers)	10.2	10.9	12.6	11.5	12.5
Brokered Deposits (number of institutions)	186	185	156	177	136
Brokered Deposits to Assets (median % for those above)	4.9	4.2	3.7	3.9	3.2

Loan Concentrations (median % of Tier 1 Capital)	Q2-05	Q1-05	Q2-04	2004	2003
Commercial and Industrial	123.2	118.2	120.1	114.4	115.7
Commercial Real Estate	192.3	189.4	167.5	178.1	154.8
Construction & Development	31.8	30.3	23.6	29.7	23.3
Multifamily Residential Real Estate	2.6	2.7	2.1	2.4	1.7
Nonresidential Real Estate	137.5	137.9	123.2	133.4	118.0
Residential Real Estate	160.6	161.4	157.5	163.1	151.7
Consumer	42.7	42.7	47.6	43.4	50.5
Agriculture	88.3	85.2	94.0	88.7	94.0

BANKING PROFILE

Largest Deposit Markets	Institutions in Market	Deposits (\$ millions)	Asset Distribution	Institutions
Minneapolis-St. Paul-Bloomington, MN-WI	178	52,380	< \$250 million	427 (90.9%)
Fargo, ND-MN	25	3,059	\$250 million to \$1 billion	38 (8.1%)
Duluth, MN-WI	33	2,968	\$1 billion to \$10 billion	4 (0.9%)
St. Cloud, MN	34	2,817	> \$10 billion	1 (0.2%)
Rochester, MN	24	2,198		